

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ORBIT GAS COMPANY)	
)	
COMPLAINANT)	
)	
vs.)	CASE NO. 9075
)	
TEXAS AMERICAN ENERGY CORPORATION)	
AND NATIONAL PIPELINE COMPANY)	
)	
DEFENDANTS)	

O R D E R

On June 6, 1984, Orbit Gas Company ("Orbit") filed a complaint against Texas American Energy Corporation ("Texas") and National Pipeline Company ("National"). Western Kentucky Gas Company ("Western") is a division of Texas. In its complaint, Orbit alleges that the proposed sale of a 65-mile natural gas transmission pipeline by National to Western is inappropriate. A hearing on the issue was held on October 25, 1984, at the Commission's offices.

The reasons given by Orbit in opposition to the transfer are that local producers now selling gas to Orbit would be deprived of a market; contracts between Orbit and two of its customers, Southwire and National Southwire Aluminum ("NSA"), will be breached; Orbit will lose a substantial portion of its business; and Orbit rather than Western should be the purchaser. None of

these matters relates directly to the issue of whether the transfer is in the best interest of Western and its customers. Orbit also suggests that Western has several alternatives to the purchase, viz. the use of the pipeline under Orbit's ownership and the upgrading of the Bon Harbor Storage Field for peak shaving purposes.

Western's position is based in part on its current gas purchasing situation with its suppliers. Those suppliers are Texas Gas Transmission Corporation ("Texas Gas") (86 percent), Tennessee Gas Pipeline Company ("Tennessee Gas") (13 percent), and Kentucky producers (1 percent). Texas Gas Zone 3 is Western's major market area and the gas purchases represent 62 percent of total company purchases. Western purchases gas from Texas Gas at 54 points within that zone.

Western purchases gas from Texas Gas under a two-part demand and commodity schedule. The demand is based on Western's contract for maximum day purchase which is 94,043 Mcf in Zone 3. Western must pay demand charges on at least 95 percent of this contract demand, and cannot exceed the contract on any one day by more than 2 percent without incurring a penalty. The commodity charge is simply a rate per Mcf for each Mcf purchased. As of September 1, 1984, the Zone 3 demand charge was \$5.93 per Mcf per month and the commodity charge was \$3.2949. Based on this rate, and a demand of 94,043 Mcf, the annual demand charge in Zone 3 is \$6,690,000.

Texas Gas changed its rate design from the United Method to the Seaboard Method on November 1, 1982. This change increased

Western's demand charge in Zone 3 from \$2.78 per Mcf to \$5.93 per Mcf. Based on a contract demand of 94,043 Mcf, Western's Zone 3 demand charges were increased by almost \$3,600,000 per year. Tennessee Gas changed to the modified fixed Variable Design and has increased its demand charge to \$7.98 per Mcf per month.

In order to reduce the cost of purchased gas, Western is attempting to reduce its peak day purchases from suppliers by the use of underground storage. On Western's peak day of December 24, 1983, 92,648 Mcf were supplied from underground storage and this much demand gas from Texas Gas would cost \$6,593,000 per year.

In addition to helping to alleviate the rising cost of gas from its suppliers, Western believes that the pipeline will provide increased utilization of its existing facilities. At present, Western does not need to develop new underground storage facilities because it has adequate storage capacity; however, Western does not maximize its capabilities due to market restrictions caused by limited pipeline facilities.

Western's largest and best storage areas are the St. Charles and Kirkwood fields in Hopkins County, Kentucky. These two fields represent 70 percent of Western's storage working gas. However, the problem with these fields is that they are limited to the Madisonville-Princeton-Hopkinsville market area because of Western's existing pipeline system. In order to realize the capacity of these fields, the market must be extended. One way to accomplish this is to connect the two fields to the Owensboro-Hawesville market.

This can be accomplished by the contract negotiated between National and Western dated May 24, 1984. The 65 miles of 12-inch pipeline is located in the heart of Western's market area, beginning in the Hawesville industrial area, crossing Western's Owensboro transmission lines and terminating close to the St. Charles Storage Field.

According to Western's testimony the pipeline will be purchased for a total cost of \$2,300,000, with \$600,000 payable at closing, and the balance, plus interest at the rate of 12 percent per annum, is to be paid for a period not to exceed 4 years and will be based upon the volume of natural gas purchased by NSA and Southwire at their Hawesville plants. The financing is attractive to Western and of benefit to its ratepayers because the additional revenues generated by the industrial sales, resulting from the purchase of the pipeline, will more than pay for all the necessary expenditures. It is estimated that it will take approximately 8 calendar quarters to retire the total indebtedness and, due to the positive revenues, the pipeline will become the property of Western at no cost to its other ratepayers.

Another advantage to Western is that the 12-inch pipeline crosses a major Texas Gas pipeline, which is operated at a high pressure. In storing gas at such a pressure, a higher pressure pipeline will allow Western to "float" gas into the storage field during most of the summer months without the use of a compressor, thus making storing gas more economical and feasible. If Western is permitted to purchase the pipeline, the ownership will also

open the potential for future purchases from American Natural Resource Pipeline and Midwestern Pipeline.

There could also be some advantage to Western in connecting its storage system to its Eastern District which is served by Tennessee Gas, through a connection with Midwestern Pipeline, which is a subsidiary of Tennessee Gas. This would offer the future possibility of exchanging storage gas with Tennessee Gas thereby reducing the cost of gas purchased in the Tennessee Gas area of Western.

COMMENTARY

In Western's original filing, certain savings were cited as reasons for requesting the Commission's approval of the pipeline purchase. These savings were based on added peak shaving capability which would reduce demand charges paid to Texas Gas and which could allow for reduced contract demand. Under cross-examination it was pointed out that the estimations used by two Western witnesses (Mr. Thomas Brady and Mr. Carl Weller) differed and that the contract demand reductions had not been approved by Texas Gas or the Federal Energy Regulatory Commission. Furthermore, the cross-examination of Mr. Brady implied that little in-depth study was conducted by Western with regard to the use of the pipeline. Several options for the use of the pipeline were mentioned and savings and increased sales were identified as positive aspects of Western's ownership of the pipeline, but concrete benefits could not be specified. The Commission is confident that Western's customers will benefit by Western's ownership of the pipeline by way of the peak shaving and

increased sales benefits. Furthermore, Western's customers should benefit from decreased gas costs resulting from Western's purchases of local production. For these reasons, the Commission is of the opinion that Western should be allowed to purchase the pipeline. The Commission strongly recommends, though, that Western prepare a better case in future transactions of this sort and puts Western on notice that it must show the peak shaving benefits and contract demand reductions in its next rate case or Purchased Gas Adjustment filing. Without sufficient evidence of savings resulting from this pipeline purchase, the Commission may disallow any costs associated with the purchase in future rate case revenue calculations.

With regard to the storage field questions raised by Orbit, the Commission is not convinced that the Bon Harbor field presented least cost peak shaving capabilities for Western. Western countered Orbit's argument about the advantages of the Bon Harbor field by specifying the allowable operating pressure changes which would be required to adequately upgrade the field and the severe safety concerns associated with very high pressure lines in or near highly populated areas. Also, under cross-examination, Orbit's witness (Mr. Jack Elenblaas) was not able to prove that the Bon Harbor field could safely accommodate the additional storage pressure required for effective peak shaving benefits. The Commission is of the opinion that Western's proposed use of the St. Charles field presents the most cost effective, safe means to improve Western's peak shaving

capabilities and that ownership of the pipeline is necessary to realize these benefits.

Western has been and continues to be strongly encouraged to purchase any and all local production which will reduce its cost of gas. Recognizing the fact that traditionally it is the producer's responsibility to deliver pipeline quality gas to the purchaser at sufficient pressure, the Commission strongly encourages Western to purchase all local production available at a delivered price less than or equal to the Texas Gas commodity rate. The Commission also encourages Western to pursue all prudent means to increase the volume of local purchases that it may make under contract provisions with its pipeline suppliers, Texas Gas and Tennessee Gas. Western has testified that it will purchase local production. The Commission shall continue to review Western's gas purchasing practices in future proceedings.

CONCLUSION

After reviewing the record, the Commission is of the opinion and finds that:

1. The contract of purchase by Western from National is self-financing. Western's ratepayers will have the benefit of a \$2,300,000 asset without participating in financing the pipeline;
2. Western's cost of gas will be reduced by additional peak shaving and by injecting gas into the St. Charles - Kirkwood Storage Fields with substantially less use of a compressor;
3. In the future, the purchase of the pipeline will open new options to purchase gas from other suppliers;

4. Western will provide the full needs of additional industrial customers;

5. The purchase will aid Western in utilizing its western Kentucky storage capacity for its eastern market area;

6. Western will be in a position to supply additional firm gas to its present and future customers; and

7. The sale of the pipeline to Western is needed and is in the public interest.

IT IS THEREFORE ORDERED that:

1. The contract between National and Western is approved; and

2. A certificate of convenience and necessity is granted.

Done at Frankfort, Kentucky, this 23rd day of January, 1985.

PUBLIC SERVICE COMMISSION

Richard D. Deman
Chairman

W. H. Dyer
Vice Chairman

Sam Shultz
Commissioner

ATTEST:

Secretary